

MINUTES
REGULAR MEETING OF THE BOARD OF LAND COMMISSIONERS
Monday, June 20 2005, at 9:00 a.m.
State Capitol Building, Room 303

PRESENT: Governor Brian Schweitzer, Superintendent of Public Instruction Linda McCulloch, Secretary of State Brad Johnson, Attorney General Mike McGrath, and State Auditor John Morrison

Motion was made by Mr. McGrath to approve the minutes from the regularly scheduled meeting of the Board of Land Commissioners held May 16, 2004. Seconded by Ms. McCulloch. Motion carried unanimously.

BUSINESS TO BE CONSIDERED

605-12 SUN RIVER ACQUISITION – FWP

Glen Erickson, Field Services Division Administrator – FWP, said this is a fairly significant acquisition, 134 acres, of prime riparian and waterfowl habitat located along the Sun River four miles west of Vaughn, along Highway 200. It is northwest of Great Falls, called the Lewis property. The site provides access on both sides of the Sun River. It is an area where we do not have any public access along the Sun River on either side for about 30 miles. Most of the proposed site is located on the south side of the river, there is a road that comes in from the north to provide access to the north side. To access to the south side people would have to either wade across the river or use a boat. It is good habitat, with upland grasslands, a large pond on the north side, and mature cottonwoods and willows along the riverbanks. Good habitat for pheasants, white-tailed deer, Hungarian partridge, antelope, and waterfowl. One of the issues that came up is that a portion of this land was used for gravel mining and processing. The property was listed as a hazardous waste site by DEQ after they discovered some 55-gallon drums of stripping paint and other chemicals buried on the land. That was removed, the riparian areas and the pond were reclaimed. DEQ ran tests at both high water and low water and all of those tests came in negative for the target chemicals they were testing for. We are now just awaiting removal of the property from DEQ's list. FWP will not purchase the property if it is not released from the contaminated site list. We have no indication that that will not happen. This acquisition was supported in the Draft EIS by the Sun River Watershed Group, the Russell Country Sportsmen Association, Missouri River Flyfishers and families in the area. An issue that came up was concerning hunting safety. This would support mostly upland bird hunting and waterfowl, we believe we can address that. The nearest house is about ½ mile away. We believe if there are significant issues that surface over time we can address them through weapons restrictions and other avenues we have available through our Fish, Wildlife and Parks Commission. Mr. Erickson requested approval for the purchase of the Lewis property, 134 acres west of Vaughn for \$150,000.

Governor Schweitzer asked if the state was taking on any potential liability in terms of ownership or did the previous owner retain some liability? Are we buying it with the understanding that if there are environmental hazards that we are not aware of that they will be held responsible?

Mr. Erickson said no. As I said before until it is released by DEQ as a contaminated site, we will not purchase the property, so therefore there is no liability for the state once it is purchased.

Motion was made by Mr. Johnson to approve the acquisition. Seconded by Mr. Morrison. Motion carried unanimously.

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Mr. Johnson asked how was the purchase price arrived at?

Mr. Erickson the purchase price is the price the owners were asking for it. We did do a market analysis and found during that review that there was an appraisal done in 1996 for \$2600 per acre. We also looked at two sales in the area near Vaughn and one near Sims that came out to \$2300 per acre and \$3300 per acre. Based upon those issues we felt \$150,000 was appropriate.

605-1 APPROVAL OF QUIT CLAIM DEED REQUEST BY DPHHS
(Dennis and Kathy Young)

This is a request for approval of a quit claim deed for property in Stanford. This has to do with a Medicaid recipient who owed DPHHS money for services and the contract was assigned to DPHHS to repay the Medicaid debt. The contract has been fulfilled and the deed would terminate DPHHS' interest and the owners title policy would be issued to the Young's. The Director requested approval.

Motion was made by Mr. McGrath to approve the request for a quit claim deed. Seconded by Mr. Morrison. Motion carried unanimously.

605-2 FINAL APPROVAL FOR TRANSFER TO JEFFERSON COUNTY (§77-2-351, MCA)

This is for transfer of three properties in Jefferson County near Boulder currently owned by the Department of Corrections. The property will be turned over for public uses. The first property will be used for the high school football field; the second is to the county for a storage site; and third the property is for the Jefferson County fairgrounds. The processes have been completed and this is the final process before turning the property over to other public entities. The Director requested approval.

Motion was made by Mr. Morrison to approve the transfer of property. Seconded by Mr. McGrath. Motion carried unanimously.

605-3 REQUEST FOR OIL AND GAS LEASE SALE APPROVAL
(Sale held June 7, 2005)

Director Sexton said we had a very successful sale on June 7, 2005. We sold 217 tracts covering a total of 97,330.76 acres; the income derived from this sale is \$1,445,329.63. The tract set aside from the first quarter sale was offered for bid at this sale and sold for \$42.00, previously it was at \$2.00.

Motion was made by Mr. Johnson to approve the oil and gas lease sale. Seconded by Mr. McGrath. Motion carried unanimously.

Governor Schweitzer asked if there were any anomalies in this sale? He said as managers of the lands, and with oil taking off as it has, and the revenue flowing like it is, is there an observation you can make or pass along to the Board in terms of prices relative to historical levels, the number of people bidding, etc.?

Director Sexton said there were some new players and quite a bit of interest in Gallatin, Park, and Meagher Counties.

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Monte Mason, DNRC Minerals Management Bureau Chief, said in general and in addition to the new players coming back into the state, you are seeing a broader interest over more counties. If you look through the lease sale there were more tracts that received bids and a lot of them were going for \$7, \$8, and \$10. In times past, you might have a "hot" county, like Richland County is now. You would see Toole County would go to the applicant because you were lucky to have one person trying to scratch out something profitable at that point in time in that county. But even Toole County was getting bids this time. What is interesting is the breadth of interest I am seeing. Obviously the totals we've got in the last two sales, \$2,000,000 and \$1.4 million this month are much higher than we've had in the past. Going back several years when oil was \$10, \$12, and \$15 we had sales where we might have only had 13 tracts that were nominated and it took us about 10 minutes to do our lease sale. This isn't quite back to the levels we had in the late 1970's but I'm told back then that some of the better sales went for two or three days and they were held in the Capitol in the House Chambers. The top one was around \$15 million, but this sale is right among our top ten. We had one sale that was \$15 million back then and a couple in the \$6 million and \$7 million range. There is interest, there are new players, and we are happy to have it.

Governor Schweitzer said what do you make of the interest in Park and Gallatin Counties? Is this coalbed methane at play?

Mr. Mason said I do not believe so. It could be some shallow gas or some deeper plays but I don't believe that commercial coalbed would necessarily go that far north. The Gallatin County tracts are east of Toston, about 20 miles.

Mr. McGrath said I am curious on #127, the one we rebid. Who came in and bid it?

Mr. Mason said the people from before did bid but they were outbid by another company.

605-4 APPROVAL OF COMMUNITIZATION AGREEMENTS

- A. Klabzuba Oil and Gas Inc.
- B. Burlington Resources Oil and Gas Company
- C. Omimex Canada, Ltd

Director Sexton said there are three communitization agreements that range from 25% to 50% interest. The first is in Hill County, the second is in Richland County, and the third is in Liberty County. Again, these are interests the state has in a larger area so we can gain our fair share of income from these parcels.

Motion was made by Mr. McGrath to approve the three communitization agreement requests. Seconded by Mr. Johnson and Ms. McCulloch simultaneously. Motion carried unanimously.

605-5 BUNCH GULCH TIMBER SALE

This proposed sale is located in Ravalli County approximately 13 air miles southwest of Darby on the Sula State Forest and proposes to harvest from 351 acres using a salvage/sanitation type harvest. This treatment is meant to recover the value of insect and diseased trees. There are 76 acres containing old growth and they will be treated in a manner that retains sufficient large live trees and the stand will meet old growth criteria under Green et al. The primary harvest is to salvage Douglas-fir killed or infested with beetles, as well as trees with severe dwarf mistletoe infections. The estimated sale volume is 10,787 tons or 1,922 MBF with an estimated minimum value of \$176,858.00. Access to the sale is across existing roads. A temporary road use permit has been obtained from the USFS. Public comment was

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solicited and issues of concern were wildlife, roads, watershed and soil. The primary public comment was on Big Horn Sheep habitat. Mitigation has been directed that will restrict periods of operation. Logging and road building activities will be allowed during the periods of January 1 – February 15 and August 1 – October 15. The mitigation measures were incorporated into the Environmental Assessment.

605-6 CELLAR GULCH TIMBER SALE

This proposed timber harvest is located 11 miles west of Canyon Creek in Lewis and Clark County. The estimated sale volume is 1,466 tons (208 MBF) with an estimated minimum value of \$22,723.00. The sale totals 55 acres. Harvest treatments proposed are an over story removal on 48 acres and an even-aged shelterwood harvest on the remaining seven acres. No new roads will be built. Access is across existing roads. Roadwork requirements include 3.14 miles of reconstruction and 1.17 miles of obliteration. Public involvement was solicited through newspaper ads, letters to interested parties and adjacent landowners. Issues of concern were noxious weeds, aesthetics, wildlife, road density, and safety. Logging equipment washing requirements prior to entering the sale area along with pre and post harvest weed spraying will mitigate the weed issue.

605-7 DRY CREEK HELICOPTER SALVAGE TIMBER SALE

This proposed harvest is located 12 miles northeast of Ovando in Powell County. The estimated volume is 7,295 tons (1,328 MBF) with an estimated minimum value of \$52,524.00. The sale totals 73 acres. The bark beetle attacks have reduced the number of live large trees to the point where they no longer qualify as old growth stands under Green et al. The salvage operation treatment will remove all merchantable Douglas-fir from all four units and lodgepole pine from unit 4 unless designated to leave. There will be .15 miles of low standard road construction to access the helicopter landing area. Access to the sale is across existing roads. Temporary road use permits from the USFS have been obtained. Public involvement was solicited and the main issues of concern were loss of security cover, impacts to grizzly bears and impacts to bull trout/west slope cutthroat trout in Dry Creek. Due to road construction there may be a short term reduction in security cover. After the sale the .15 miles will be gated. Access to the harvest units is by foot traffic or helicopter only. The main concern was for impacts detrimental to threatened and endangered species. These were mitigated by requiring the use of helicopter yarding, minimal new road, no motorized activities near Dry Creek on other than existing open roads, and requirements for sanitation and safety procedures when operating in the area to limit interactions with grizzly bears.

605-8 LONE TREE PASS LIMITED ACCESS SALE

This proposed harvest is located 65 air miles southeast of Dillon in Beaverhead County. The estimated volume is 6,197 tons (925 MBF) with an estimated value of \$103,428.00. The sale totals 168 acres and is partially a salvage harvest responding to bark beetle attacks. Approximately 130 acres would be harvested under a prescription to allow for the development of old growth characteristics. Old growth is present on 38 acres. A restoration prescription would be utilized on these acres to maintain the old growth. The proposed project would move the older stands to more historic conditions while retaining the old growth attributes of the existing stands. Access to the sale is across private land. The landowners have agreed to allow limited access until September 30th. The landowners will only allow Sun Mountain Lumber to have access to conduct a timber harvest. There will be 2.5 miles of new road construction. The road would be rehabilitated after use. Public involvement was solicited through newspaper ads, letters to interested parties and to adjacent landowners. The main issues of concern were wildlife and

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wildlife corridors, threatened and endangered species, water quality, increased truck traffic on local roads, new road construction and old growth. Mitigation measures were incorporated. This sale was proposed at an earlier date but because of the amount of roads to be built, it was not.

Ms. McCulloch said her office had a concern come in about making sure this project would be finished by duck season.

David Groeschl, DNRC Forest Management Bureau Chief, said this sale was never actually proposed before the Board, there had been some initial scoping and public comments were gathered. Originally there were 13.2 miles of road that would have been needed to be built with a bridge, now we're looking at less than 2 miles of road coming across private lands. The landowner is willing to allow us through his property to have the sale completed by October 1st. The end of September is when the sale must be completed.

Ms. McCulloch said so you will be out by duck season?

Mr. Groeschl said yes.

605-9 WOODS CREEK TIMBER SALE

This proposed harvest is located six miles northwest of State Highway 434 near Wolf Creek in Lewis and Clark County. The estimated volume is 5,412 tons (761 MBF) with an estimated minimum value of \$74,811.00. The sale totals 126 acres. This is a salvage operation because of beetle infested trees. Access is across existing roads. A temporary road use permit granting permission to cross private lands has been obtained. There will be .20 miles of road construction, 2.11 miles of spot road reconstruction, and .20 miles of reclamation. Public involvement was solicited through newspaper ads, letters to interested parties and adjacent landowners. The one issue raised through the scoping process was protection of existing fencing. Resource and property damage responsibilities are addressed in the timber sale contract.

Director Sexton requested approval of the above described timber sales.

Motion was made by Mr. Johnson to approve the package of timber sales. Seconded by Ms. McCulloch. Motion carried unanimously.

605-10 LAND BANKING SALE APPROVAL

Director Sexton said in April the Board approved 609 acres, and in May we had the largest group of proposals which was 22,694. This month we have approximately 900 acres. This will finish the first grouping of land banking proposed sales. These are located mostly in central and western Montana. The first one was lessee nominated by the Meyer Ranch Company, in Powell County. It is 640 acres isolated by the Meyer Ranch. The second one is in Flathead County and was department-proposed. There is no current legal access, a close road provides physical access through the Flathead National Forest. At this time DNRC is finalizing a reciprocal access agreement with Plum Creek to grant them access across the subject parcel due to an adjacent 40-acre parcel. There is no legal access. The next is 80 acres in Lake County. A subdivision would be very costly in this area.. There is low potential for development or value added activities at this time. This is lessee nominated and is surrounded by lessee-owned land. The final parcel is in Flathead County, 100 acres in Section 36 within the City of Kalispell. In this section

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there is a Lowes store, a Costco is under construction, the high school is in part of Section 36, the ball field recreational field is there already. This is a residential area and it is proposed for residential use. Most of the other projects in Section 36 are leased projects. Single family lots are not marketable as a lease. Developmental activities are limited to those that can be achieved within the current land banking authorization. We recommend the consideration of the sale of the land after securing preliminary subdivision entitlements in partnership with a private firm. We would be compensated for this property based on the raw land value plus we would share income from development. The Mayor of Kalispell is in support. This is the kind of development within city limits that makes sense for the community and also makes sense for trust revenue.

Mr. McGrath said the Binger Lease is on reservation property, has the tribe expressed any interest in this or has the department had any discussions with them about the potential that we might be selling this property?

Tom Schultz, DNRC Trust Land Management Division Administrator, said I am not aware of any specific interest by the tribe. I think there is a global interest in acquiring land within the reservation. This particular tract is surrounded by private land. The tribe could theoretically bid on the tract but they would have to get access through the private landowner.

Mr. McGrath said I have a request, would the department notify the tribal council or somebody in the tribal government on this? Just to make clear, what we're taking about today is just for preliminary approval that we are identifying parcels.

Ms. Sexton said that's correct. After this we will go through the cultural process, it will be appraised and brought back to the Board to determine the minimum bid. Then after the public auction takes place, the Board will approve it. So there is a three-step process and this is the first step in that process.

Mr. Morrison asked who does the department anticipate the buyers to be? And for those lands that we anticipate will be subdivided, are we selling these parcels in their entirety to somebody who will then go about the subdivision process? Or is there going to be further parceling off of these pieces by us? We have the 100 acres in Section 36, the 80 acres near Lake Mary Ronan, the 80 acres in Lake County. Any of it that is subject to potential subdivision?

Ms. Sexton said we hold those parcels that are probably less likely to have development on them. The one surrounded by forest has no access. The others are lessee-nominated and are wholly surrounded by the lessee so access would be a problem. We would not at this point in time anticipate development, if that does occur that will roll into what we have as limits as far as subdivisions as proposed in the Programmatic EIS. As far as I know except for the parcel in Kalispell, we are not expecting development on these parcels.

Mr. Morrison said who do we expect as a buyer say for the 80 acres of timber property in Flathead?

Ms. Sexton said with the national forest access there, that could be a recreational person and it could mean the ability to develop that and perhaps they will have to go through the planning process. For any subdivision you have to prove lawful access before you can do any subdividing.

Mr. Morrison said who is going to buy 80 acres of isolated timber in that area?

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Mr. Schultz said this question came up at the staff meeting and we have not been notified by anybody who has expressed interest in it. There are three or four adjacent landowners who might have interest. This is one that we don't have a guaranteed buyer. We could go through the process and put it up for bid and there may be no interest. We don't actually know at this point. It's likely there could be interest, but we don't have access to the tract. If an adjacent landowner had access to the tract, perhaps. My understanding is it is a rocky area and there are no good building sites on it. I think it is suited more for recreation. We don't have a person lined up. Regarding the tract in Kalispell, we should talk about the process a little bit. We haven't done this before where we've actually partnered with somebody. Regarding the 640 acre tract in Kalispell, there are 60 acres of it in Phase I. The Board approved the lease of about 17 acres and that is where the Lowes is and the Costco is being built. This tract sits on the southwest corner and within that is the eastern half of that quarter. There is a bypass that goes through the section. The part of the section we are talking about is everything east of the bypass. It is 100 acres and we anticipate if we get approval we will put an RFP together and solicit a bid. There will be three parts; first they will have to put a bid on the bare land value which is between \$20,000 and \$30,000 per acre now; they would have to put in an option, much as we did with the high school which paid a 1% option and we would anticipate something like that to hold it; they would then have to act within 9 – 12 months and break ground and carry forth on the option. If they don't act on the option they would forfeit the money they put on the option and we would retain the land. If they do act on it the option money would go toward paying the actual cost of the sale. The third part they would bid on, the state would then secure some share in the final development of lots. When we developed the lots in the Billings area, we did the whole process. We went out for sale on individual bids, we actually had to bid those lots out. That process was a cumbersome process and in the end we didn't make out much better. In this process we would work with the developer up front, we would share in that final revenue. So, we would get the bare land value and any improved value for the land once the entitlements, sewer, water, etc., were brought up to the houses. We would also get maybe 5% to 10% of the value of those lots. We would be partnering with developers. Mr. Goldberg who developed the Section 36 so far is very interested in this, there is another man from Billings who is also interested and there could be other developers who are interested. But that is how that process would work.

Mr. Morrison said will we retain an interest in the value that is accrued from the subdivision? This is going to wind up being worth more than \$20,000 or \$30,000 per acre.

Mr. Schultz said that's correct. It could be \$5,000 to \$10,000 per lot or it could be a share. It might be more appealing to the developer as a share because the lots could go for \$40,000 to \$50,000 per lot. We will be learning as we go through the process. But we are very concerned about capturing the enhanced values with the entitlements.

Governor Schweitzer said on sale #202, the 80 acres, the State of Montana has decided to nominate that. What was the process that said that's the one?

Mr. Schultz said the process was the local field offices look across the landscape at the land we are managing. Tracts that we typically don't have access to, that aren't producing any revenue, those are tracts that we've historically looked at. In Eastern Montana its much the same way. We look at tracts that are isolated and the field is looking for tracts that are headaches to manage. It could be a five-acre tract, a 10-acre tract, or a 40-acre tract. In many cases you can't even locate that tract within a section because it is not surveyed. Its the same thing in Western Montana. There are tracts that we typically don't have access to or ones that don't generate any revenue. This is a tract that hasn't generated any revenue in some time and we don't have access to the tract. That was the driving force.

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Governor Schweitzer said but we have an ongoing negotiation with Plum Creek to grant them access and vice versa.

Mr. Schultz said yes and that is not complete yet. We are in negotiations with them now to gain access, right now there is no access. The other piece is, we need to generate revenue from the higher end parcels to make landbanking work. You talked last month about appreciation. This is a tract that we think could have higher value than the \$100 to \$200 per acre range we will see in Eastern Montana. I am not sure what this could go for but its probably not unreasonable to say \$1,000 to \$5,000 per acre for that ground. If we're going to have enough money in the pot to purchase tracts that we all want, that have public access, that have increased revenue value we do need to have some of the higher value tracts in Western Montana. So it's a combination of we haven't generated revenue off of this in the past, it's a tract that does have potential for higher value, and we don't have access to it currently.

Mr. Morrison said on the map we have on Sale #202, it is next to private ownership and Forest Service and Plum Creek. Have we ever cut timber on this? Why do we own that little piece of land?

Mr. Schultz said my guess is that at one point we owned the whole section and it is possible it was sold off. If you look at the sections around it there are many whole sections but you'll see a couple of quarters and halves. At one point we probably had more than just those 80 acres.

Mr. Morrison said this is inaccessible to us because we can't go across the Forest Service land, we can't go across the private land, and the Plum Creek is isolated too.

Governor Schweitzer said so what are we trading them for?

Mr. Morrison said the person is going to want this is the person who owns the rest of that section, right?

Mr. Schultz said I don't think it is just one landowner that owns the rest of the section, it is multiple landowners within Section 36 whose land abuts the state section that want to purchase the state tract.

Mr. Morrison said as we start down this landbanking road I am just trying to get a feel for how these things are going to be working.

Mr. Schultz said the predominate focus is on tracts we don't have access to. And tracts in Western Montana are the ones we think we could have some increased values so we could buy something. We will sell 15,000 acres in Eastern Montana at \$100 per acre, that's only \$1.5 million and not a lot of money to buy something. So that is why this Section 36 in Kalispell, the 100 acres, has potential for significant revenue to make the whole project have enough money in the bank to actually purchase land. We do have to start on some of these smaller acreages on the west side to make this work.

Mr. Morrison said this is land we have not cut timber on? At least for a long time?

Mr. Schultz said not for a while. I am looking at that rate of return and my guess is there is probably some grazing going on, the rate of return is 1.3% which is pretty low.

Governor Schweitzer said in the future he hopes that when we are getting ready to do some land banking and we have ongoing negotiations regarding access I'd like to have that as part of the file to know where

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we are and where those roads might be and what private entities are getting out of the easement reciprocal.

Mr. Schultz said we could postpone this until next month and come back with the information you're asking for to make a more informed decision. If you would like to do that we can.

Mr. Morrison said I second what Governor Schweitzer said about that because while I trust the department in these matters it is particularly important to the public that as we dispose of any pieces of state land that we know exactly who is potentially benefiting and who has a stake in it. That has to be part of the evaluation whether to separate anything from the trust. The other question I have is we did approve a couple of preliminary sale proposals last month, four or five, and what prospects do we have so far for identifying land to buy with the proceeds? I ask that partly because I want to make sure that the buying is part of the process and I ask it partly because under the rules of course we can only have 20,000 acres separated from the trust at any one time and then we are frozen. What's our prospects?

Ms. Sexton said we do have Item #605-15 Land Banking Acquisition yet to discuss and I hope to go through the rules that were set up for acquisition and also to gain your input. There is time set aside for information on acquisitions, where we are, and where we wish to be.

Motion was made by Governor Schweitzer to approve all the sales with the exception of Sale #202, the 80 acres, pending more information on the proposed easements. Seconded by Mr. McGrath.

Mr. Johnson said given the fact that we are so early in the process and we will revisit these proposals at least two more times before final decisions are made I am not sure we need to hold that one out. If the information comes back at the next meeting raises further questions, we can withhold approval at the next juncture.

Governor Schweitzer said I think that is a good point, we are very early in this process and we are building this process as we go along. I would like the staff to understand that before they bring this at the beginning of these processes if there is an ongoing negotiation with private or other public entities about easements that that ought to be part of what the Board reviews at the head end of this not at the middle end. If it holds us off for another month on an 80-acre piece I for one would think it would be appropriate.

A vote was taken on the motion. It carried unanimously.

605-11 RIGHTS-OF-WAY APPLICATIONS

This month there are fourteen requests for approval of rights-of-way application. Ms. Sexton said most of these are historical requests. She suggested there was one application from Teton County which I believe does cross a riverbed and it would be inappropriate for us to grant access that crosses the Teton River where you would have to drive through the river. As far as I know the others are fairly straightforward and I didn't see any issues.

Lisa Axline, DNRC Rights-of-Way Coordinator, said the application that Director Sexton is speaking to is #13530 for Peter and Kathy Balasky. The Balasky's own some property in Teton County, a portion of which is cut off by the north and south forks of the Teton River. The state land adjoins their private property on that side and there is a county road that currently traverses through the state property. There

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is a two-track trail that goes across the state to the border of our property with the Balasky's. There is a crossing of about 350 feet on that. The Balasky's were requesting a private driveway easement to access that isolated parcel that is isolated by the river so they could build a future cabin there. It did not fall under our historic process. The river, both the north and south fork of the Teton, actually falls on the Balasky's private property. They are not crossing any river crossing that would be on the state tract. I am not quite sure if I understood from Director Sexton if the issue was they would be utilizing that state road to eventually cross the river to gain access to the rest of their property.

Ms. Sexton said they have done that through a state piece and they have been crossing the river illegally.

Ms. Axline said I spoke with our Conrad Unit Office this morning and it was their understanding that they were only going to use this road on the state tract as a secondary type of access to get to that isolated parcel so they could run their cattle. There was no intention for them to cross the river according to our Unit Office. We could certainly stipulate in an easement to them that they cannot ford the river illegally or that they would have to get permits.

Ms. Sexton said is this from the north?

Ms. Axline said I am not sure.

Ms. Sexton said I asked about this last week and I haven't gotten any answer to it. I would suggest that that one be withdrawn now and we can clarify it and bring it back next month. Otherwise I would like to withdraw that application for rights-of-way.

Ms. Axline said it makes no difference to us at this point. The Balasky's actually live in Florida and are here in Montana part time. We could certainly withdraw that and revisit the issue if Director Sexton would prefer.

Ms. Sexton said it would be my suggestion that #13530 be withdrawn from consideration until next month until the issue is clarified.

Mr. McGrath moved the rights-of-way applications be approved with the exception of #13530. Seconded by Ms. McCulloch.

Governor Schweitzer said it says this is a private access road to a single family residence but then I also heard that it was for livestock reasons.

Ms. Sexton said and I am not sure. They have built a bridge to access their property that's why I am not sure what the need of this is. I have heard there are problems with them illegally crossing state property, crossing the river to access their property. I am concerned that this not be an invitation for an illegal crossing the river.

Governor Schweitzer said given that this is in your county, do you know this piece of land and the people as well?

Ms. Sexton said yes I do.

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Governor Schweitzer said if at any time in the future you would like to recuse yourself in any of these proceedings, or you think it is necessary, you just let us know.

A vote was taken on the motion to approve the rights-of-way applications with the exception of #13530. It carried unanimously.

INFORMATIONAL ITEMS

Ms. Sexton said what I am going to try to do at each meeting is the issues that arise during discussion that the Board has questions about, we will do research and present them at the next meeting. That is why there are four of these informational issues on the agenda today. The first is the rental rate adjustment for metalliferous leases.

605-13 RENTAL RATE ADJUSTMENT – METALLIFEROUS LEASES

Ms. Sexton said Attorney General McGrath brought this topic up last month. We can, under the existing rules, change the initial lease from \$1.00 to \$3.00. We can do that within the scope of the rules. Mr. Mason did some research into what other states do. Wyoming charges \$1.00 for the first five years then it goes up to \$2.00; North Dakota does no leasing; South Dakota charges \$1.00 which is fixed throughout the time period of the lease; Idaho charges \$1.00 fixed; and Colorado charges \$3.00 fixed. We would now have \$3.00 the first year, \$1.00 the second and third year, \$2.50 the fourth and fifth years, and then \$3.00 after that for a 10-year average of \$2.50. Again, this arose from our discussion at the last meeting and our proposal is that the department should require the first year rental be \$3.00/acre in future leases.

Mr. Morrison said what do you project that means in terms of revenue for us?

Ms. Sexton said minimal.

Ms. McCulloch said this rate doesn't need to be approved by the Board?

Ms. Sexton said no, the department can do it under the existing rules. If the Board wants to increase it more, it would mean a rule change.

Ms. McCulloch said you wouldn't increase it or decrease it without bringing it to the Board for approval?

Ms. Sexton said if it were increased, and we contemplated a rule change?

Ms. McCulloch said the Board didn't have to approve the increase from \$1.00 to \$3.00. The department can change the amount without bringing it to the Land Board?

Ms. Sexton said on future leases we will bring them to you and suggest the lease rate be \$3.00 for the first year.

Ms. McCulloch said my question though is if the Board doesn't have to approve this rate, does that mean that the department can change the rate on their own without coming to the Land Board?

Ms. Sexton said I think we'd have a recommendation that would come to the Land Board.

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Mr. Mason said that's correct. The thing to point out is that this would be our policy on the standard rental rates that we would bring to the Board. Obviously every lease we issue comes to the Board for approval. If there were any concern that the rates we were proposing were too low or too high, the Board would have the authority to change that. This is just a general policy that the Board can expect the great majority to come to you with this rental rate.

Ms. Sexton said this is in response to a concern that Attorney General McGrath expressed last month.

Mr. Johnson said he had two questions, one is what is the rationale in these variable rates? I see Colorado has established fixed rates. Also when were these current rates established? How long has it been since we've visited those?

Mr. Mason said its been at least 20 years, since the last time rule changes were done on this particular issue. The rationale behind the escalating rental rate in general is that it serves as some form of encouragement for the lessee to explore and find something because his holding costs will increase over time if he doesn't do anything there. It becomes more expensive for him to hold that lease. You see that in oil and gas leases. How much of an incentive it is would be open to debate. You see some other states with fixed rates, but that is general process of the thinking behind an escalating rate.

Mr. Johnson said in the scheme of things today, we look at all of the costs associated with the developing one of these mine sites. Is the difference between \$1.00 and \$3.00 per acre really material today?

Mr. Mason said not if they find something commercial it isn't. The key thing to remember is this is incredibly speculative. The rental rate reflects that because basically it has no value unless they explore and develop. It is meant to be enough of a holding cost that it doesn't inhibit their ability to spend capital on exploration but also be enough that if they are just somebody out of state holding onto the lease because they want something in Montana, it doesn't cost them to do that. It's a balance.

Mr. Johnson said what's the average size of one of the parcels leased under this program?

Mr. Mason for metalliferous I am guessing 160 acres, a quarter section on average.

Governor Schweitzer said just so we understand what will occur in the future is you will come to us with a proposal and your recommendation will be \$3.00, and we can make a determination as we go forward.

Ms. Sexton said that's correct.

605-14 CONSERVATION OPTIONS

Ms. Sexton said we've been discussing this for the last couple of months. I asked our staff attorneys to come up with a greater in-depth analysis of conservation options for trust lands. Mark Phares, attorney for trust lands and forestry, wrote an extensive analysis and we've just included the executive summary in the packet. The entire analysis was sent to you electronically. The complete analysis includes what conservation options in trust lands we have, what sort of leeway we have, what opportunities we have, and how cut and dry are our opportunities on the landscape. We did include with this what we have done in the past on conservation leases and licensing, and also the language we have changed for the programmatic EIS regarding conservation options which is broader than the previous language. There is

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in your packet today the summary of licenses we have issued in the past without a conservation option to them. This was to further broaden the opportunities for conservation on trust lands.

Mr. Morrison complimented Mr. Phares on his excellent work on the analysis. He said I appreciate your doing it, you have addressed the issues and given us some good guide posts for going forward. I am optimistic that we're going to be able to effectuate the Whitefish plan given these options.

Governor Schweitzer said he'd like to echo that. Mr. Morrison speculated that we may have more authorities than we had been exercising in the past. I appreciate the work you have done, it is important for us to know what our options are.

Ms. Sexton said to follow up on that, she met with the Whitefish group a couple of weeks ago exploring what projects they had in mind. It was very fruitful. They are looking at opportunities at Spencer Mountain right now and they would like to come to the Board meeting in September or October and give an informational update on their activities. I have shared with them the information on conservation options.

605-15 LAND BANKING ACQUISITION

Ms. Sexton said the next issue for information was land banking acquisition. Auditor Morrison talked about this. I would point you to the one sheet in the packet, the one after the administrative rules, we have a draft tract evaluation for trust land acquisition. The issues such as is the tract an easement or improvement? How it will be classified? There are a lot of very common sense practical questions as we analyze a tract. I understood that the Board members wanted some sort of hands on ability. My suggestion to you is as I come around to visit with you individually and talk about the Programmatic EIS we could perhaps talk about your thoughts regarding acquisition. Or if you would like, as part of a Board meeting have a work session where we solicit you for what criteria you'd like to look for in purchasing property. Either way would be fine with the department. What we do this first time around will be key to the long term success of the viability of the program so I would like to proceed in a manner that gives you and the public optimum input in how we go about selecting parcels for acquisition. What is the Board's pleasure? Whether we have a work session where we discuss criteria, standards, guidelines, or acquisitions, fitting within the rules we already have, or would you like me to just visit with you individually about your own interests?

Mr. Morrison said we need to air that discussion here. So whether it happens first at the staff level and then comes here or whether the department comes forward here is up to you. Generally things work better when you get together and sort this out at the staff level and then come here with a presentation. I think having a discussion in this open forum about that very important issue is appropriate and necessary.

Mr. McGrath said I would agree. I think that I've reviewed the checklist and it is very good and I have already contacted you about certain parcels that I think we ought to look at trying to acquire. I think that Board members should work with the staff to identify those. But obviously this needs to be a transparent process. I don't think we need a work session but we need a transparent process.

Ms. Sexton said I hope to make appointments with each of you and your staff members over the next month to go through the Programmatic EIS and to discuss the acquisition process. Maybe from that I can have a list of approaches and can bring that to the next meeting for discussion so we know what types of

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tracts you are looking at. Is it a single tract? Is it two or three different ones? Is it in different parts of the state? I'd like to have some criteria and guidelines from you.

Mr. Morrison said clearly the key part will be the outreach. Getting the criteria out to people across the state because there is undoubtedly hundreds of people who care a lot about this issue and know about parcels we might not be aware of.

Ms. Sexton said we have already been working with brokers and exchange specialists and I have gotten a number of phone calls from individuals who have property they would like to nominate.

605-16 CASH LEASES ON AG TRUST LANDS

Ms. Sexton said this issue arose at the last meeting. We did include in the packet a summary of activities. In the past there was legislation proposed in 1997, a copy of that proposed legislation is attached. As stated in the summary, a fairly small percentage of our ag land, less than 7%, is a cash lease the rest is share crop, one quarter of the annual crop, not less than one quarter. We do have 170 agricultural leases that have been converted to cash but that is a relatively small portion of all of our ag leases. The proposed legislation was modeled after a North Dakota process using the Montana Ag and Statistics to determine the average cash rental rates for each county. Previously the concern for the legislation was how would you reach the county average and how accurate would it be and would it be a benefit to the lessee as well as to the trusts. This information is available.

Governor Schweitzer said when this proposal has come up in the past, resistance was from the farmers who were on a crop share basis. Was it the resistance from the producers themselves that doomed this legislation?

Kevin Chappell, DNRC Ag and Grazing Bureau Chief, said generally it was. It was our lessees. Primarily it was Daniels County that has always resisted in the past. The reason being is that you are well aware of the land ownership the state has in the western portion of that county and so operators in western Daniels County have a large percentage of state leases. That is a large component if not a total component of their operation. So, basically we were shifting the risk to them entirely and they were not interested in having that take place. So they have been the primary ones in the past that have come in.

Governor Schweitzer asked how many FTEs does it take to follow each producer? As you know they are required to give you a planting report sometime in the spring and then fill out some forms that show they have purchased hail insurance or crop insurance, and then they have a crop production report that comes in after they harvest. How many people does it take to track these reports?

Mr. Chappell said for the reports that are generated, those come out of the Helena office and are mailed to our lessees, both the seeding report and the production report. Those all come back to our office as well. We have one person on my staff who receives that information and enters it into our computer to store and account for payments. Copies of those reports are also forwarded out to each of our area and unit offices. They take those and they are the ones who determine where they want to follow up. They may look at ones that may be chronically low and they may go out and monitor those during the field season. I have one person who does the actual physical receiving of the reports and the money and the field office then decides from that information where they want to spend their time monitoring.

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Governor Schweitzer said in addition to that, the field office often spends time at the FSA offices going through the maps to look at the reporting to make sure they are consistent. To make sure that what has been reported as planted at the FSA and to make sure it is consistent with what has been reported to the State of Montana.

Mr. Chappell said that is correct. And then they are signing up with the farm programs on a share basis. The state is entitled to a share of the annual program payments that come from the county FSA offices. So they are involved in all of that paperwork, signing that up, and as a follow up they will go into the county offices, the FSA offices, and confirm information as well when it is necessary.

Mr. McGrath said the department has the authority, or the Board as the authority, to adopt a policy. It could just go to a cash lease process. Is that your understanding? Or do you think we need legislation?

Mr. Chappell said the way we've looked at it is, if you look at the legislation and §77-6-501, MCA, it states the renewals would be made on a crop share basis and that the department can convert them to a cash basis. So we've interpreted that by law we have to issue a lease on a share basis of not less than one quarter and if the lessee is interested in converting it into a cash, and we can negotiate and come up to an agreeable rate between the two of us, then we can convert it. We've interpreted that you can't issue it on a cash basis.

Mr. McGrath said what about Subsection 2.? And the bill that is crossed out? Mr. McGrath said it says except in the case of a cash lease, renewals under Subsection 3, if it is in the best interest of the state, the department may authorize a lease upon other basis than crop share.

Mr. Chappell said I guess we read that in conjunction with the first part which states first we issue them on a share and then if you want to issue them on a cash that it would be between the lessee and the state negotiating that.

Mr. McGrath said I know there are certain members of this Board who think it is in the best interest of the state that we have a cash lease. Do you have an opinion on that?

Mr. Chappell said I would agree with that. Every two years as we think about proposed legislation through the EPP process we talk about whether we think the time would be appropriate for cash leasing again. Unfortunately during times of drought and low commodity prices that makes that sale harder. So for the last several sessions we've decided not to try to pursue it. But the department has always been a supporter of cash leases and we try to convert to cash leases whenever we can. If this Board is interested in doing that we can have those discussions and think about it for the next legislative session. I guess where we've probably failed a little bit in the past also is we probably didn't get out and talk with some of those folks on the front end about what we were proposing and how the process would work. So if we want to do that I think it would be important for us to get up to Daniels County and meet with those folks and talk about options and see if they have changed their mindset. Before 1997 when we proposed this, we had almost no cash leases with any of our lessees up there now. That has changed quite a bit since then. We've had folks come around and they are interested in doing cash leases. So a number of ones I report here do come from Daniels County.

Governor Schweitzer asked how many individuals do we have crop share arrangements with now? What is the number of people plus or minus a few thousand?

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Mr. Chappell said we have roughly 3,000 – 3,500 leases that include crop lands on them. As you can see in the report we've only got about 170 that are on a cash basis. So it is a fairly small percentage.

Mr. Johnson said do you know what the total acreage is for the ag leases? The 31,270 represents just those 170 cash leases?

Mr. Chappell said roughly for agricultural lands it is around 570,000 acres. That includes crop land, hay land, and also lands enrolled in the Conservation Reserve Program. They have about 140,000 acres in CRP.

Mr. Johnson asked have you been able to determine what kind of physical impact it would have if we converted those 570,000 acres that are currently under share lease to a cash basis?

Mr. Chappell said we haven't done it recently. When we looked at it in 1997 for the legislation, we thought it would be at least revenue neutral or if not increase our revenues off of our ag lands. It depends upon the type of system you'd want to look at. Currently for FY-04 we generated about \$8.4 million off of our ag land, roughly \$17 per acre. I think we ought to be around \$17 - \$20 per acre.

Mr. Johnson said that \$3.00 difference between the \$17 and the \$20 that is the average for these 170 leases over ½ million acres is real money.

Mr. Chappell said I think if we ran numbers today that's where we would shake out.

Ms. Sexton said we can certainly do that analysis and bring it back to the Board next month.

Governor Schweitzer said I would hope the Board would agree with me that we should ask the Attorney General for an opinion as to whether we have the unilateral right to convert these to cash based on the language we currently have.

Mr. McGrath said I don't think we need a formal opinion but I will ask Candy West to work on that and maybe Mr. Phares you or Mr. Butler can give us a memo on that as well and then we'll put something together for the next meeting.

PUBLIC COMMENT

Roy Andes, MonTRUST, said I want to thank the Board for its concern about all of these informational items. I particularly want to say a couple of things about the cash lease/crop share issue. This has been a concern of ours for some time, and back when I used to work for the Department of State Lands, virtually every local land office had horror stories about the kinds of things people would do to a state paying legitimate crop share including things like sending the bad loads of grain to the sale first and calling it the state's share and then sending the good loads later. I think we all in this room share the concern for the possibilities that cash leasing would open up to us, so we would full heartedly endorse your efforts in that respect.

Ms. Sexton said for your information we held roundtable discussions with our stakeholders about a month ago on trust lands, the past, present, and future. We divided into two different working groups working on two issues that were of most interest to folks at the discussion. One issue was public outreach and public information. There was quite a bit of concern expressed that people in Montana don't understand

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what trust lands are about, their purpose, how they are managed, where they are going in the future. We have one working group made up of a broad array of stakeholders who will be focusing on giving us advice about how we can better reach the public and how we can also better educate the public. A second group is made up of university people, MonTRUST, conservation groups, and commodity groups all interested in how we can address the many interests of our stakeholders and interest groups regarding public access, grazing, ag, and timber while we enhance revenue for the trusts. The second working group will delve into that complex issue. The two working groups will be convening and working on those two topics.

Governor Schweitzer moved to adjourn. Seconded by Mr. Morrison.